

FORTUNE
SMALL BUSINESS

Ways to
Beat a
SNEAKY
TAX
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Hidden Risks

Think buying a franchise
is safer than starting a
business? **THINK AGAIN.**

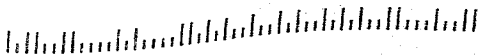
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Roger McCabe, 61,
owner of five Meineke
shops in the Midwest,
is doing well but found
franchising tougher
than he expected.

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SOMETIMES, CRITICS SAY, FRANCHISORS ARE TOO clever for their own good. Consider the strange tale of how Snap-on, the tool company in Kenosha, Wis., may have tripped over its own cocktail napkin, so to speak. Snap-on sells sales routes to franchisees, who also buy a special van and an inventory of tools. A couple of years ago Matt Setser had enough of his old job at FedEx and decided to move his family 1,100 miles, from Fort Smith, Ark., to the Tampa Bay area, to take on a route that, he says, a Snap-on franchise representative had assured him (never in writing) would gross \$30,000 a month.

As soon as he set foot on Florida soil, Setser—whose wife, Suzanne, was expecting their second child at the time—knew something was wrong: The district manager who showed him around started commiserating about what a lousy route Setser

had been sold. Fast-forward a year, and sure enough, the route paid almost nothing, Setser says, despite his long hours of work and worry, in large part because too many other Snap-on routes had been sold (at \$30,000 a pop) right in his backyard.

But here's the twist: Somebody at Snap-on may have given the game away. When the Setsers first got to the Tampa area, they rented an apartment. Because they weren't local, the landlord asked for some evidence from Matt Setser's employer of his projected income—and because Snap-on was the closest thing to an employer that the couple had, Suzanne called Snap-on and got that \$30,000-a-month figure committed to writing. The Setsers decided to give up on a losing proposition last fall; Matt now sells real estate. But their former landlord had filed Snap-on's fax predicting Matt's route would yield \$30,000 a month, and Suzanne

So You Want to Franchise Your Business?

By JUSTIN MARTIN

OTHERS FRONT THE MONEY and do the hard work while you sit back, watch your brand grow, and collect a tidy royalty stream from your franchisees. It sounds like a can't-lose proposition, but does franchising truly make sense for your small business? Like most ventures, franchising is far harder than it appears, so before succumbing to its easy-riches allure, ask yourself some tough questions.

For starters, does your business occupy a genuine niche?

"Many businesses," says Michael Seid, a West Hartford, Conn., franchising consultant, "are simply one-market wonders." Not Pizza Patrón, a restaurant chain founded by Antonio Swad, a man who knows how to carve out a niche and build up a franchise. Swad previously grew Wingstop, a chicken-wings-only restaurant, to 100 locations before selling it in 2002. His current project is even more precisely targeted: pizza for Hispanics. Swad opens Pizza Patróns only in heavily Hispanic communities, such as North Oak Cliff in Dallas, the city where the chain is headquartered. The menu features toppings such as jalapeños and chorizo, served while salsa music and reg-

gaeton—a type of Spanish-language hip-hop—play in the background. Pizza Patrón, which began franchising in 2003, has 51 locations and expects \$20 million in chainwide revenues this year. "The restaurant industry is so competitive," says Swad. "I knew I needed to offer some sizzle, not just another Pizza Hut."

Does your business have a workable financial model?

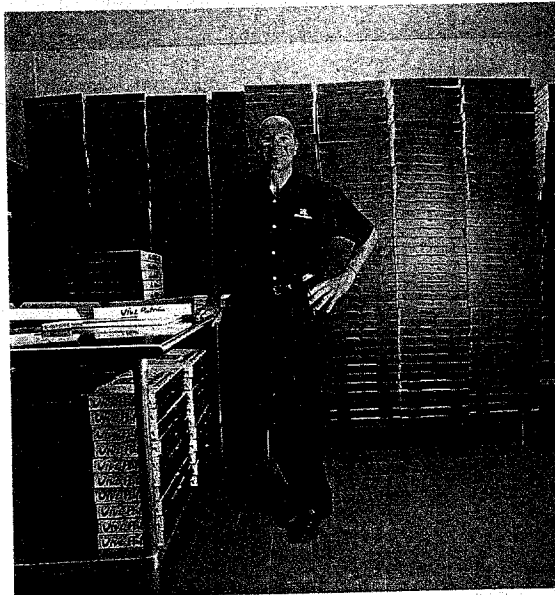
Richard Cole founded Geeks on Call, a

to attract potential franchisees—a very delicate balance.

Coles went for a modest (by franchise standards) \$60,000 initial investment, which covers training and advertising. Because he provides substantial support to franchisees, including a dedicated call center, he knew his royalty would need to be high for the industry: 11%. With the right balance of fees in place, Geeks on Call has been able to expand to 294 franchises in 25 states. "You can't do well unless your franchisees do well," says Cole.

Are your techniques easily teachable?

The success of a franchising operation can often depend on the founder's ability to translate his methods into a blueprint that franchisees can really use. Frank Fiume started i9 Sports in 1995 based on a quirky observation: "Amateur sports are run very unprofessionally." Fiume organizes leagues for adults and kids in everything from softball to flag football to lacrosse. Before franchising his business in 2003, he compiled a 500-page manual that lays out



Swad built a niche with his Hispanic pizzerias.

Norfolk outfit that dispatches techies to small businesses and homes to fix computers, in 1999. When he decided to franchise, he figured he needed a franchise fee structure high enough to fund expansion and provide profits, yet low enough

everything from how to attract players to how to obtain insurance coverage. "You want to provide every ounce of your formula," says Fiume, whose Tampa company has 50 franchises and hopes to generate \$3 million in revenues this year. □

had the presence of mind to ask for a copy. It is now an exhibit in a class-action suit of Snap-on dealers against the franchisor.

Nor is this the first time Snap-on and its franchisees have crossed swords. A Snap-on dealer in New Jersey named Brian Casey says he ran into the same trouble with Snap-on that the Setsers did. Last summer an arbitrator awarded Casey \$314,000 in damages. Says Gerald Marks, the Red Bank, N.J., franchise attorney who represented him: "Snap-on's policy of 'more feet on the street,' which places too many dealers too close together, is ill-conceived and a financial disaster."

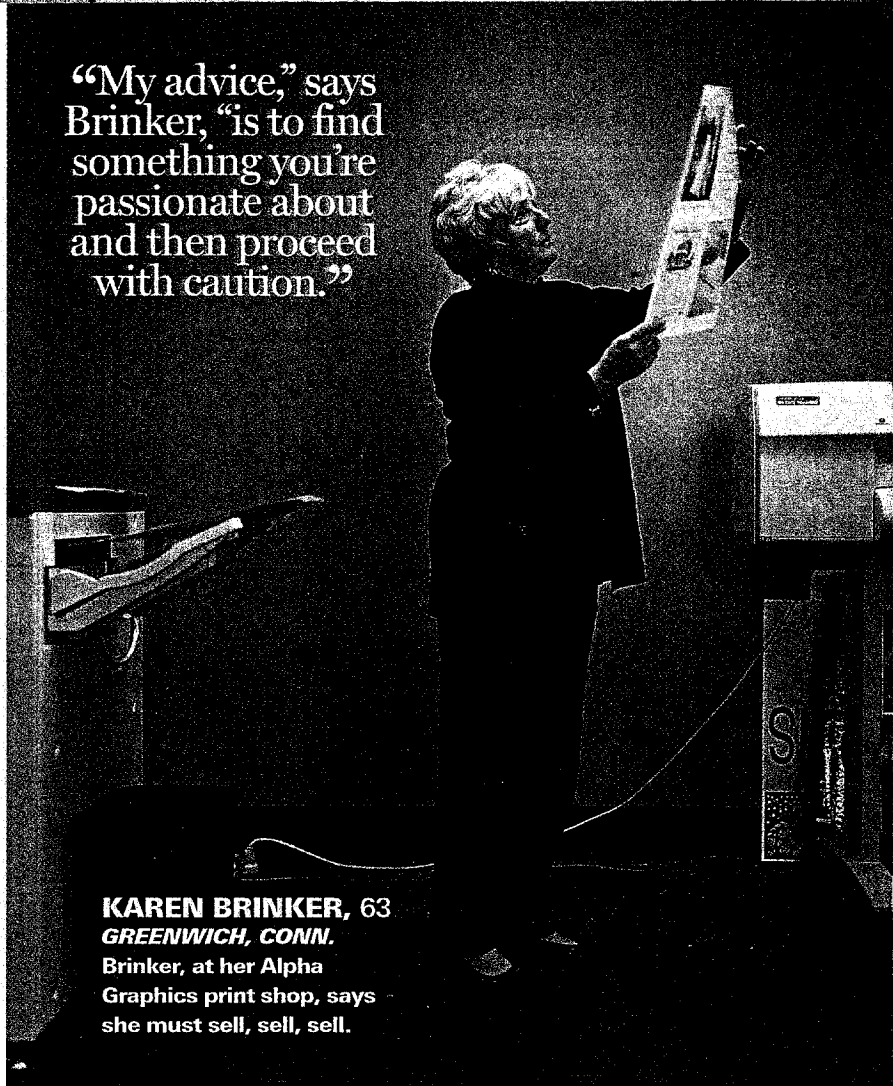
A Snap-on spokesperson responds that "a franchise is like any other business in that there is no guarantee of success." A company statement reads that before any franchisee signs on the dotted line, he is given plenty of information. Snap-on provides contact data for all active dealers in any given region, as well as for franchisees who have left the system in the previous 12 months. In other words, do your homework, then decide.

More often than not, it seems, companies that sell franchises are so much more sophisticated than the buyers that the franchisors hold most of the cards. A couple of nonprofits are trying to change that. One, the American Franchise Association, is pushing for legislative changes that could help protect—or at least alert—hordes of the unwary. Another, the Association of Franchisees and Dealers, has a set of standards—for example, franchisors may not strip franchisees of their constitutional right to a jury trial—intended to make franchising fairer. That's nice, but it's likely that the rule for would-be franchisees will be caveat emptor for years to come.

CORPORATE REFUGEES AND FORMER BUSINESS owners who have succeeded at franchising—and yes, there are thousands—suggest you do thorough research on the territory you're thinking of entering. When Terry Tryon bought his Tutor Time day-care franchise in Wyomissing, Pa., a few years ago, after 30 years at Aetna and other insurance companies, he pored over his market's demographics. "I looked at statistics from the U.S. Department of Labor on the rising need for child care in two-income families, and then I looked at this part of Pennsylvania to see what demand was and who my competitors were likely to be," he says. "A gut feeling is fine, but the more knowledge you have, the better off you are." Tryon adds, "I also talked to lots of other franchisees, both some who had succeeded and some who had failed. I got more insights from the ones that failed."

A foolproof way to get to know a franchise intimately before you invest is to get a job in one of its stores, which is what Tiffany Newman has done. An Army veteran who served in Desert Storm, Newman has spent the past few months scooping ice cream and supervising fellow employees at a Cold Stone Creamery shop in Mamaroneck, N.Y., which she says has given her "a hands-on understanding of the system here." Newman is weighing the pros and cons of either starting a catering company or buying her own

"My advice," says Brinker, "is to find something you're passionate about and then proceed with caution."



**KAREN BRINKER, 63
GREENWICH, CONN.**
Brinker, at her Alpha Graphics print shop, says she must sell, sell, sell.

Cold Stone franchise. At the moment she's leaning toward the latter. She's impressed with the thoroughness of the training as well as the support the franchisor offers.

Once you decide on a franchise—if indeed you do—be ready to sell, sell, sell. Karen Brinker, who left a marketing career in the apparel division of Playtex and used her severance pay to buy an AlphaGraphics print shop and web-design franchise in Greenwich, Conn., says the first thing she did was to "go out knocking on doors. I wore out a lot of shoe leather. You really need to be ready to do that—at least until you can hire someone else to do it." After a decade in business, Brinker says of her 6,000-square-foot shop, with annual revenues of more than \$2 million, "I love what I do here every day. My advice would be to find something you can get passionate about, and then proceed with caution."

One more thought: If you have lots of creative, original ideas about how to start and grow a business, franchising probably isn't for you. "Franchising is built on a system, and the system works if you follow it," says Slender Lady CEO Bruce Sharpe. "But one of the biggest causes of franchise failure is that people go off on tangents—they spend more than they need to on the initial facility, they don't budget enough for ads, and so on. If you don't want to follow the system the franchisor has set up, then buying a franchise is insanity." Indeed, it would be a waste of both the franchisor's time and money and your own. □

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